

INTERface

towards promoting accountability

Vol.VII

Issue IV

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an yield of 10 % on its investment in the
Rs. 5,00,000 for ten years. Lease
equation:

$$\frac{x}{(1 + 0.1)^n}$$

Table 2 : Schedule of debt repayments

End of year	Interest plus principal payment	Principal amount owing at the end of year	Annual Interest @ 16%	Principal component
Rs.	Rs.	Rs.	Rs.	Rs.
0	89,127	4,10,873	-	-
1	89,127	3,87,486	-	89,127
2	89,127	3,60,357	65,740	23,387
3	89,127	3,28,887	61,998	27,129
4	89,127	2,92,382	57,657	31,470
5	89,127	2,50,036	52,622	36,505
6	89,127	2,00,915	46,781	42,346
7	89,127	-	40,006	49,121
8	-	-	32,146	56,981
9	-	-	23,029	64,055
10	-	-	13,688	71,125
			(36,988)	(17,125)
				<u>2,87,878</u>

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Between Us

FOUR I' S PRINCIPLE

The load they carried was stunning. The discipline they have is out of the world. The dedication to the task was fascinating.

We were having a meal outdoor in a village. Some bread dropped off the plate on the ground. There they came, marching towards us like a well disciplined army. They carried the piece of bread with so much skill that some of the greatest management gurus would like to learn from them.

No wonder the Bible says in proverb 6:6 that we should look at the ants and learn from them. Their faith, determination and united effort are a source of immense encouragement to many. It is amazing that one of the smallest creatures can become a great teacher.

A *Attitude of Initiative*

Ants don't need a commander to tell them to get started.

N *Nature of Integrity*

Ants work faithfully and need no outside accountability to keep them doing right.

T *Thirst for Industry*

Ants work hard and will replace their anthill when destroyed.

S *Source of Insight*

Ants store provision in summer because in winter they may not be able to work.

Initiative, Integrity, Industry and Insight (4 I's) are so important in life and that is what ants teach us.

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FMSF.

Accounting and Reporting

- C.A. Pooja Bagga, FMSF

The Financial Reporting is an integral part of an organisation as it is an important link in the chain of Accountability. In this article we are dealing with the details about the financial reporting for a non- profit organisation

The financial statements of an organisation represent the performance of the organization in financial terms both in corporate as well as non-profit forms of organisations. The accounting practices which are followed by a non-profit organization (NPO) are generally driven by the requirements of the Income Tax Act and Foreign Contribution (Regulation) Act. There are no specific formats prescribed by any other statutory body for the reporting of the finances of a non profit organisation unlike a corporate which has to report in the formats prescribed by the Companies Act, 1956. However, the Institute of Chartered Accountants of India, through its Technical Guide for Not-for Profit Organisations has prescribed certain formats for financial reporting .

The non profit sector may follow any one of the following system for accounting i.e.

- Cash
- Accrual
- Hybrid

But in most cases, the NPOs follow Cash Basis of accounting. NPOs in absence of clearly prescribed formats, have no uniformity of presentation of financial statements. They also follow different disclosure practices and accounting policies rather than a common one. It is due to this fact that the various stakeholders are not able to use the financial statements for comparative and analytical purposes. We also need to say that the diversity of the sector and the programmes are also a limitation to evolve financial reporting formats

In view of the above and due to the nature of activity of a non profit organisation, it is very important for the organization to have their financial statements as transparent as possible to their stakeholders. The various stakeholders like:

- The Beneficiaries,
- The Board,
- The Donors,
- The Statutory bodies

rely on the financial statements along with the activity reports of the organization to understand the progress of the organisation.

The need for financial reporting is to create a link in the chain of the accountability. It also helps the various stakeholders especially the Governing Board, the donors and other statutory bodies to take decisions on the basis of the financial reports.

The need for financial reporting is to create a link in the chain of the accountability.

The non-profit sector not only comprises of the organizations like a Society, Trust or a Company under section 25 of the Companies Act, 1956, which do charitable activities but also Government run agencies like Electricity Board, Port Trusts etc.

In general, the basis of accounting followed by most of the charitable organisations in India is double entry system. However, certain government organisations still follow the single entry system of accounting.

There are two types of reports an NPO generally prepares. They are:

- Internal reports
- External reports

The Internal Reports are more process oriented and help the management and the accounts department in preparing the external reports. The internal reports are used by the Governing Board, Project Staff, Finance Staff and the General Management. They represent the systems and processes of an organization.

The Internal Reports which can be prepared by an organisation are:

- Budget Variance Report;
- Cash Flow Statement;
- Investment Status Report;
- Legal Compliance Report;
- Inter- Project Adjustment and Allocation Statement;
- Grant Status Report;
- Management Letter by Auditor;
- Internal Audit Report;

The preparation of these reports are at the discretion of the management or the decision making body of the organization.

The external reports are the financial reports which are used by the Government, Donors, Project Beneficiaries & the Society at large.

The External Reports which conform to the statutory requirements of the Income Tax Act, The Foreign Contribution (Regulation) Act (FCRA), Donors reporting

and other statutory bodies are:

- Auditors' Report;
- Balance Sheet with relevant schedules ;
- Income and Expenditure Account;
- Specific Fund Utilisation Statements;
- Receipts and Payments Account;
- Donor reporting in specified formats;
- Form FC3 for a FCRA registered organization.

Both the Internal and the External Reports help in various processes like the planning for new projects and for the control mechanism of the organisation.

The external financial reports are the mirror of an organisation. These reports should be prepared and presented to the various stakeholders in a true and fair view as duly certified by the auditor of the organization. The external reports should be comparative in presentation i.e they should provide the figures of the previous year along with the current year's figures for easy comparison by any stakeholder.

The external financial reports are the mirror of an organisation.

These external reports are:

- Receipts and Payments Account and;
- Income and Expenditure Account;
- Balance Sheet;

1. Receipts and Payments Account

The account summarizes all the actual receipts and the payments made during the financial year by the organisation. The figures are taken from the cash and

Receipts and Payment Account for the year ended 31st March 20XX

Receipts	Amount	Payments	Amount
Opening Balance - Cash - Bank Donations Grants - Local Contribution - Foreign Contribution - Government Grants Interest -Local -Foreign Funds Loans Sale of Asset		Programme Cost - Activities cost - Program staff salaries - Program administrative costs General Administrative Expenses Closing Balance - Cash - Bank	
Total		Total	

the bank book. No distinction is made between revenue and capital nature. It is a reflection of the actual inflow and outflow of the funds.

A sample receipts and payments account looks like this:

2. Income and Expenditure Account:

Income and Expenditure is a statement of accounts which basically is an activity report of the organisation but in financial terms. It is similar to the profit and loss

account prepared by organisations other than non-profit organisation and instead of profit /loss it reflects the surplus/deficit .However, while preparing the Income and Expenditure account due care should be taken that all expenses pertaining to the accounting year/period should be accounted for.

In the income and expenditure account, the transactions of capital nature whether receipt or expenditure should be taken directly to the Balance Sheet's Assets/ Liabilities column. The Deficit/ Surplus as per the Income and Expenditure account should be transferred to the

Income and Expenditure for the year ended on 31st March 20XX

Expenditure	Amount	Income	Amount
Programme Expenditure Administrative Expenditure Depreciation Audit Fees Surplus carried to balance sheet		Grants - Foreign Grants - Local Grants - Government Grants Donations Community Contribution Bank Interest Income from Investments Deficit carried to Balance sheet	
Total		Total	

General Fund Account in the Balance Sheet. This statement is very important for the stakeholders as it acts as a link between the activity report of the organisation and provides the financial figures of the activities undertaken during the year and should correspond to each other.

3. Balance Sheet

Balance Sheet presents the financial state of the organisation on a particular date. It provides the stakeholders the financial status of the organisation in concise form. The balances of the Receipt and Payments Account i.e the closing cash/bank balance and the surplus/deficit as per the Income and Expenditure Account form part of the Balance Sheet.

The balance sheet is a very important statement as it provides various information in one glance as to:

- **Reserve and Funds:** What reserves are held in the form of general fund, trust funds, corpus fund and also from various donors, programmes
- **Earmarked funds:** The status of the earmarked funds and their utilization as on date.
- **Loans and Advances** details of the organisation
- **Cash and bank balance** as on the date.
- The details of the **fixed assets** etc.

It is recommended that the balance sheet and also the other financial statements should be prepared in a comparative form so as to provide a comparison between the previous year and the current year to analyse the changes made during the year.

A sample format of Balance Sheet as at 31st March 20XX is provides below:

BALANCE SHEET AS AT 31ST MARCH 20XX

LIABILITIES	Amount	ASSETS	Amount
Long Term Funds		Fixed Assets	
Current Funds		Investments	
Current Liabilities & Provisions		Current Assets, Loans, Advances & Closing Stock	
Total		Total	

It is also a very important tool to ascertain some of the financial ratios to realize relationship between two figures.

- Compliance of FC(R)A.
- Contingent liabilities;
- Previous year figures.

It is very important that along with the above financial statements the auditors also provide with relevant accounting policies on the following:

- Fixed Assets;
- Depreciation;
- Foreign currency transactions;
- Investments;
- Grants receivables;

This helps the various readers of the financial statements understand the statements more clearly.

It is also very important that the organisation prepare these financial statements every financial year as firstly it is a statutory requirement and its compliance mandatory but also it is a away the organisation can be more transparent and accountable to its various stakeholders.

An Overview of the Minimum Wages Act, 1948

- Ruhy Narang, FMSF

1. Introduction

The Minimum Wages Act is a welfare legislation in favor of the workers and is a measure for the economic upliftment of the workers in the sweated industries. The Act falls within the scope of Entry 27 in list III of Schedule VII of the Constitution of India.

2. Object and Purpose

The philosophy of the Minimum Wages Act and its significance in the context of conditions in India has been decided by the Supreme Court in **Unichoyi Vs State of Kerala** as follows:

“What the minimum wages purports is to prevent exploitation of labor and of that purpose authorizes the appropriate Government to take steps to prescribe the minimum rates of the wages in the Scheduled industries. In an underdeveloped country which faces the problem of unemployment on very large scale, it is not unlikely that labor may offer to work even on starvation wages. The policy of the Act is to prevent the employment of such labor in the interest of the general public and so in prescribing the minimum rates the capacity of the employer need not be considered. What is being prescribed is minimum wage rates which a welfare state assumes every employer must pay before he employs labor.

3. Objective

The objective of the Act is to provide for fixation of minimum rate of wages in certain employment. The employment is of those which are included in the schedule and are referred to Scheduled employment. The Act applies to whole of India.

Before we look into the various aspects relating to minimum wages, it is important to understand the meaning of some of the important definitions:

4. Important Definitions:

4.1. “Appropriate government” means -

- (i) in relation to any scheduled employment carried on by or under the authority of the Central Government or a railway administration] or in relation to a mine oilfield or major port or any corporation established by a Central Act the Central Government and
- (ii) in relation to any other scheduled employment the State Government;

4.2. “Competent authority” means the authority appointed by the appropriate government by notification in its Official Gazette to ascertain from time to time the cost of living index number applicable to the employees employed in the scheduled employments specified in such notification.

4.3. “Cost of living index number” in relation to employees in any scheduled employment in respect of which minimum rates of wages have been fixed means the index number ascertained and declared by the competent authority by notification in the Official Gazette to be the cost of living index number applicable to employee in such employment.

4.4. “Employer” means any person who employs whether directly or through another person or whether on behalf of himself or any other person one or more employees in any scheduled employment in respect of which minimum rates of wages have been fixed under this Act and includes except in sub-section (3) of section 26 –

- (i) in a factory where there is carried on any scheduled employment in respect of which minimum rates of wages have been fixed under this Act any person named under clause (f) of sub-section (1) of section 7 of the Factories

Act 1948 (63 of 1948) as manager of the factory;

(ii) in any scheduled employment under the control of any government in India in respect of which minimum rates of wages have been fixed under this Act the person or authority appointed by such government for the supervision and control of employees or where no person or authority is so appointed the head of the department;

(iii) in any scheduled employment under any local authority in respect of which minimum rates of wages have been fixed under this Act the persons appointed by such authority for the supervision and control of employees or where no person is so appointed the chief executive officer of the local authority;

(iv) in any other case where there is carried on any scheduled employment in respect of which minimum rates of wages have been fixed under this Act any person responsible to the owner for the supervision and control of the employees or for the payment of wages;

4.5. "Schedule employment" means an employment specified in the Schedule or any process or branch of work forming part of such employment;

4.6. "Wages" means all remuneration capable of being expressed in terms of money which would if the terms of the contract of employment express or implied were fulfilled be payable to a person employed in respect of his employment or of work done in such employment and includes house rent allowance but does not include -

- (i) the value of –
 - a) any house accommodation, supply of light, water medical attendance or

b) any other amenity or any service excluded by general or special order of the appropriate government;

(ii) any contribution paid by the employer to any person fund or provident fund or under any scheme of social insurance;

(iii) any traveling allowance or the value of any traveling concession;

(iv) any sum paid to the person employed to defray special expenses entailed on him by the nature of his employment; or

(v) any gratuity payable on discharge;

4.7. "Employee" means any person who is employed for hire or reward to do any work skilled or unskilled manual or clerical in a scheduled employment in respect of which minimum rates of wages have been fixed; and includes

1. an out-worker to whom any articles or materials are given out by another person to be made up cleaned washed altered ornamented finished repaired adapted or otherwise processed for sale for the purposes of the trade or business of that other person where the process is to be carried out either in the home of the out-worker or in some other premises not being premises under the control and management of that other person; and
2. an employee declared to be an employee by the appropriate government; but does not include any member of the Armed Forces of the Union.

5. Minimum Wages

The Act does not define the term and concept of

minimum wages. According to the Act, minimum wages should not only include bare sustenance of life but also it should be adequate to preserve the efficiency of workers. The other mandatory components, which have to be considered, are education, medical requirements and amenities of workers. They have to be paid irrespective of the paying capacity of the Industry.

5.1. Fixation of Minimum Rate of Wages (Section 3)

Section 3 of the Act lays down that the appropriate Government shall fix the minimum rate of wages payable to employees in an employment specified in part I and part II of the Schedule.

In case of the employments specified in part II of the Schedule, the minimum rates may not be fixed for the entire State. However, in case of an employment specified in part I, the minimum rate of wages must be fixed for the entire State and no part of the State being omitted. The rates to be fixed need not be uniform. Different rates can be fixed for different zones or localities.

5.2. Manner of fixation

According to Section 3(2), the 'Appropriate Government' may fix minimum rate of wages for:

- (a) Time work, known as a Minimum Time Rate;
- (b) Piece Work, known as a Minimum Piece Rate;
- (c) A "Guaranteed Time Rate" for those employed in piece work for the purpose of securing to such employees a minimum rate of wages on the time work basis.
(This is intended to meet a situation where operation of minimum piece rates fixed by the appropriate Government may result in a worker earning less than the minimum wages), and
- (d) An "Over Time Rate" i.e. minimum rate whether a time rate or piece rate to apply in substitution for

the minimum rate which would otherwise be applicable in respect of overtime work done by employee.

Section 3 (3) provides that different minimum rates of wages may be fixed for-

- (a) different scheduled employments;
- (b) different classes of work in the same scheduled employments;
- (c) adults, adolescents, children and apprentices;
- (d) different localities.

Further, minimum rate of wages may be fixed by any one or more of the following wage period, namely;

- (a) by the hour;
- (b) by the day;
- (c) by the month, or
- (d) by such other large wage period , as may be prescribed.

In case the rates are fixed by the day or by the month, the manner of calculations of such rates may be indicated.

In light of the fixation and revision of minimum wage, the system works as a two tier structure, which is at Central and State level. At Central level it is taken by Central Industrial Relationship Machinery and at State level it is the responsibility of the respective State Government.

5.3. Minimum Rate of Wages

According to Section 4 of the Act, any minimum rate of wages, fixed or revised by the appropriate

Government under section 3 may consist of –

- (i) a basic rate of wage and special allowance at rate to be adjusted , at such intervals and in such manner, as the appropriate Government may direct to accord as nearly as practical with the variation in the cost of living index number applicable to such worker (herein after referred to as the cost of living allowance) or;
- (ii) a basic rate of wages with or without the cost living allowance and the cash value of the concession in respect of supplies of essential commodities at concessional rates where so authorization; or
- (iii) an all inclusive rate allowing for the basic rate, the cost of living allowance and the cash value of the concessions, if any.

The cost of living allowance and the cash value of the concessions in respect of supplies, essential commodities shall be computed by the competent authority at such intervals and in accordance with such directions specified or given by the appropriate Government.

5.4. Procedure for Fixing and Revising Minimum Wages (Section 5)

In fixing minimum rates of wages in respect of any scheduled employment for the first time or in revising minimum rates of wages, the appropriate Government can follow either of the two methods described below:

5.4.1. Committee Method [Section 5 (1) (a)]

In this method Committees and Sub Committees are set up by appropriate governments, to hold enquiries and advice with regard to fixation and revision of wages. The appropriate Government shall, by notification in the official gazette, fix or revise minimum rate of wages. The wage rates shall come in to force, either from specified date in the

notification or on expiry of three months from the date of issue of notification..

5.4.2. Notification Method [Section 5 (1) (b)]

When fixing minimum wages under section 5 (1)(b), the appropriate Government shall by notification, in the Official Gazette publish its proposals for the information of the persons likely to be affected thereby and specify the date not less than 2 months from the date of the notification, on which the proposals will be taken into consideration.

5.5. Minimum wages- whether to be paid in cash or in kind

Section 11 of the Act provides that the minimum wages payable under the Act shall be paid in cash. But, where it has been the custom to pay wages wholly or partly in kind, the appropriate Government, on being satisfied, may approve and authorize such payments. Government can also authorize for supply of essential commodities at concessional rates. Where payment is to be made in kind, the cash value of the wages in kind or in the shape of supplies of essential commodities on concessions is to be estimated in the prescribed manner.

5.6. Payment of Minimum Wages is Obligatory on the Employer (Section 12)

Payment of less than the minimum rates of wages notified by the appropriate Government is an offence. Section 12 lays down that the employer shall pay, to every employee engaged in the Scheduled employment under him, such wages at a rate not less than minimum rate of wages fixed by the appropriate Government under section 5 for that class of employment without any deduction, except as may be authorized, within such time and subject to such conditions, as may be prescribed.

It is pertinent to note that the liability of the employer to pay minimum wages fixed under the Act is mandatory liability and it is not possible for the

employer to evade or escape from his liability under the Act. Section 12 of the Act create and impose obligation on the employer. Section 25 of the Act, relating to contracting states that no employee can enter into any contract with the employer relinquishing his right to minimum wages under the Act nor can he in any way, surrender any privilege or concession or even reduce his rights conferred upon him under this Act. Section 20 (3) (i) provides that if any employer pays to his employee wages at the rates less than the rates fixed under the Act, the Competent Authority can recover the amount of difference in the wages along with a compensation which may extend up to ten times of the amount of difference.

5.7. Fixing hours for a normal working day etc. (Section 13)

The provisions of section 13 are designed to prevent any exploitation of the employee employed in the Scheduled employment. The minimum wages fixed under the Act are payable to the employee for a particular duration of work and therefore the Government is empowered to fix the number of hours of work which may constitute a normal working day, otherwise it might be possible for the employer to extract more work from the employees requiring them to work for longer hours and the very purpose of the Act would be defeated.

Therefore, it is laid down that if the employer extracts the work from the employee beyond and in excess of normal working hours, he shall pay the over-time wages to the employees for that excess work.

While fixing the number of hours of work which shall constitute a normal working day, Government can also fix one or more intervals, day of rest in every period of seven days which shall be allowed to all the employees and payment of wages for such rest –days.

However, if the employee is required to work on a day of rest he shall be entitled to the specified over-time

wages as fixed by the Government.

5.8. Payment of Overtime (Section 14)

Section 14 provides that where an employee, (whose minimum rate of wages is fixed under the Act by the hours, by the day or by such longer wage period as may be prescribed,) works on any day in excess he shall paid at the overtime rate as may be fixed under the Act or under any other law of the appropriate Government for the time being on force whichever is higher.

5.9. Wages of a worker who works less than normal working day (Section 15)

If the rate of wages has been fixed under the Act by the day for an employee and if he works on any day on which he is employed, for a period less than the requisite number of hours constituting a normal working, he shall be entitled to receive wages for that day as if he has worked a full normal working day.

It is provided that he shall not receive wages for full normal working day-

- (i) if his failure to work is caused by his unwillingness to work and not by omission of the employer to provide him with work.
- (ii) such other cases and circumstances, as may be prescribed.

5.10. Steps taken by Centre to reduce disparity in wages.

5.10.1. Regional Committees: India is a huge country and there exist differences in the minimum wages paid in various regions of the country. Another reason for disparity is that both the Central and State governments are appropriate bodies to fix, revise and enforce minimum wages in their respective jurisdictions. At present there are five regional Minimum Wages Advisory Committees in the

country which are as:

- Eastern Region
- Northern Eastern Region
- Southern Region
- Northern Region
- Western Region

5.10.2. National floor level Minimum wage: In order to have uniform wage structure and to reduce

the disparity in minimum wages across the country, concept of National Floor Level Minimum wage was mooted on the basis of the recommendations of National Commission on Rural Labour (NCRL) in 1991. Keeping in the view of NCRL and with considering the subsequent rise in price indices initially in the year National Floor Level Minimum Wage was fixed at Rs.35/ per day in the year 1996. Based on the norms suggested by working group and its acceptance by the Central Advisory Board in its meeting in the year 1993 ,National Floor Level Minimum wage has last been revised upwards to Rs.65 / per day with effect from 1.02.2004.

Minimum Wages for Scheduled Employments, Central Govt.

S.n.	Name of Employment	Minimum wages per day (in Rs.)
1	Agriculture	107.78
2	Construction/Maintenance of Roads and building operations	67.43
3	Maintenance of Buildings.	67.43
4	Construction/Maintenance of Runways	67.43
5	Gypsum mines	67.43
6	Barytes mines	67.43
7	Bauxite mines	67.43
8	Manganese mines	67.43
9	China Clay mines	67.43
10	Kyanite mines	67.43
11	Copper mines	67.43
12	Clay mines	67.43

13	Stone mines.	67.43
14	White Clay mines	67.43
15	Ochre mines	67.43
16	Fire Clay mines	67.43
17	Steatite mines	67.43
18	Asbestos mines	67.43
19	Chromite mines	67.43
20	Quartzite mines	67.43
21	Quartz mines	67.43
22	Silica mines	67.43
23	Magnesite mines	67.43
24	Graphite mines	67.43
25	Felspar mines	67.43
26	Red Oxide mines	67.43
27	Laterite mines	67.43
28	Dolomite mines	67.43
29	Iron Ore mines	67.43
30	Granite mines	67.43
31	Wolfram mines	67.43
32	Magnetite mines	67.43
33	Rock phosphate mines	67.43
34	Hematite mines	67.43
35	Marble and Calcite Mines	67.43
36	Uranium mines	67.43
37	Mica mines	67.43
38	Employment in Lignite mines	67.43
39	Gravel mines	67.43

40	Slate mines	67.43
41	Employment in laying down of underground electric, wireless, radio, television, telephone, telegraph and overseas communication cables and similar other underground cabling, electric lines water supply lines and sewerage pipe lines	67.43
42	Loading, unloading in Railways goods shed	67.43
43	Ash pit cleaning in railways	67.43
44	Stone breaking and Stone crushing	87.24
45	Security services	70

The State Governments are persuaded to fix minimum Wages such that in none of the scheduled employments, the minimum wage is less than National Floor Level Minimum Wage. To some extent this method helped to minimize the disparity in wages.

It is also noted that the Central Govt. also decides schedule employments, for which minimum wage is fixed, under the minimum wages act, 1948 . They are as follows:

5.11. Offence and Penalties

Penal provisions are contained under section 22, 22A, 22B, 22 C and 23 of the Act.

5.11.1. Penalties for Certain Offences

Any employer shall be punishable with fine which may extend to six months or which may extend to Rs. 500 or with both, who

- a) Pays less than minimum rate of wages fixed for the employees, class or work or less than the

amount due to him under the provisions of the Act; or

- b) Contravenes any rule or order made under section 13 i.e fixing hours for a normal working day, etc.

Section 22 provides that while imposing fine under the section, the Court shall take into consideration, the amount of compensation award under section 20 by the Authority while dealing the claim of the employer.

General provisions for punishment of other offences-

Section 22 A provides that if any employer contravenes any provision of this Act or any rule or order made thereunder, shall, if not other penalty is provided for such contravention by this Act, be punishable with fine which may extend to Rs. 500

5.11.2. Cognizance of Offence

To enable a court to take cognizance of a complaint

under the Act, it is provided in section 22 B (i) that the complaints should be sanctioned by the appropriate Government, if it is made under section 22a, by an inspector if it is made under section 22 b or under section 22A. Further, the complaint under section 22(a) and (b) is required to be made within one month from the date of grant of sanction and under section 22A within six months from the date on which the offence is alleged to have been committed.

5.11.3. Bar on Suits

Section 24 provides bar to entertain suits by the Courts for recovery of wages in so far as the sum so claimed falls within any of the following categories:

- (i) For which an application of claim has been presented under section 20 by or on behalf of the penalty;
- (ii) Direction of the claim has already been given;
- (iii) The amount adjudged in any of the above proceedings is not due the penalty; and
- (iv) The amount could have been recovered by making application under section 20 to the authority.

The Minimum Wages Act, 1948 provides for a full-fledged procedure for the settlement of claims arising out of the Act under section 20 and penalties for any violation of the Act under section 22, it is laid down that no court shall entertain any suit for recovery of wages in so far as the money so claimed forms the subject of an application under section 20, or any direction under that section.

6. Conclusion

Despite the various efforts made by the Central Government to form minimum wage to eradicate inequality, there are some workers organizations which are demanding for framing of a "National Wage Policy". This is due to absence of some elementary needs which are not considered while determining minimum wage. Some scholars believe that most serious distortion in wage determination was related to non- adoption of the premise "wage for the worker and his family; As once stated by Mr. Sharma, former chairperson of the National Commission for Scheduled Castes and Scheduled Tribes, "It is a mystery how the crucial elements of family got omitted in the Directive Principles of State Policy while framing the Constitution, that even the highly 'eulogised' National Rural Employment Guarantee Act has adopted the same norm while envisaging the minimum wage at "not less than Rs. 60 per day as against the requirement of Rs. 133 per day for bare subsistence. In the same issue there are few scholars who believe that, evolving a National Wage Policy based on principles of ensuring a minimum wage to all employed, rationalizing wage differentials and making wage adjustment functional has been widely recognized. Though it is desirable to have a National Wage Policy it is difficult to form one, because of number of factors like agro-climatic conditions, local conditions, cost of living, paying capacity which varies from state to state and Industry to Industry. It is a daunting task to maintain uniformity in wages.

To improve the conditions of deprived, and those who work for unorganized sector the biggest task ahead is to form a system where both the above problems can be overcome by taking lessons from the countries where "National Wage Policy" is implemented.

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Accumulation of Income

- S. P. Selvi, FMSF

Voluntary Contributions, grants from donor agencies, membership fees are some of the primary source of funds for the Voluntary Organizations. These funds are meant to be spent by the Voluntary Organizations towards achieving its objectives.

Owing to this, many argue that these funds are not an organization's own funds or its income, as the organization acts only as a conduit whereby it enables the funds to fulfill the social cause for which the organization is existing.

1. Income of an Organisation

However, under the ambit of Section 11(1) through Section 12(1) of the Income Tax Act, 1961, the grant-in-aid received by a voluntary organization is treated as income of the organization. According to an author¹, *"the intention of the law is to treat income in a more general, commercial and popular sense than giving it a technical meaning."*

2. Exemptions & Deductions

While the Income Tax Act aims to levy tax on the "income" of a voluntary organization, it also provides exemptions and deductions subject to compliance of some conditions. This is stated in Section 11 of the Income Tax Act, 1961.

Some of the conditions are :

- a. the organization must exist mainly for a social benefit, which can be religious or charitable in nature.
- b. the organization must be registered under section 12A of the Act with the Commissioner of Income Tax.
- c. the organization must get its accounts audited

if its income exceeds the minimum exemption limit. For the year 2005-06, the minimum exemption limit is Rs. 1,00,000.

- d. the organization should not undertake any business activity for the sole purpose of making profit. However, if such activity is incidental to the attainment of its aims and objects, it is allowed under the Income Tax Act, 1961. Separate books of accounts for such activities are required to be maintained.
- e. the organization should apply (spend) atleast 85 % of the income of that year in the same year.

Now, looking into the condition as per point e, the natural question that comes in our mind is, what happens if an organization is not able to spend 85% and its related implications.

Let us take an example.

An organization has received grants amounting to Rs. 1,00,000 in the year 2006-07. As per the above condition, it needs to spend Rs. 85,000 (which is 85% of Rs. 1 lakh) in the same year itself. This implies that the organization will not be levied tax for the 85 % it has spent.

What happens to the remaining 15% i.e., Rs. 15,000? The other question is, what happens if the organisation has not been able to spend 85% of its income in the same year?

3. Accumulation of Income

Section 11(1) (a) and Section 11(1) (b) states that an organization can accumulate upto 15% of its income for indefinite period. In the above example, the organization can accumulate upto Rs. 15,000 for indefinite period.

¹ Manoj Fogla in Taxmann's Taxation of Trusts & NGOs

In case the organization has spent less than 85%, i.e., if it has spent only Rs. 65,000, then accumulation of 15% of the income which is Rs. 15,000 can be made. The remaining Rs. 20,000 can still be accumulated by applying to the Assessing Officer in Form 10 under Section 11 (2) within the prescribe time frame.

This extra accumulation can be made for a period of 5 years, which means that this Rs. 20,000 has to be spent with the period of next 5 years. It is also important to state in Form 10 (while applying for accumulation of income) that the accumulated income will be spent only for charitable purposes. Application of income as per this section does not permit transfer of funds to any other charitable organization.

Apart from the above, there are certain other provisions related to accumulation, which are :

* we had seen above, the provision relating to spending 85% of the income received in a specific year in the same year itself. This is in case of the income received by the organization. What happens if the income is accrued but not received ? In such instances, the organization has to take the consent of the Assessing Officer, to consider the income accrued but not received as deemed application.

For example, if an organisation's income is Rs. 75,000 of which it has received only Rs. 50,000, then with the consent of the Assessing Officer, the unavailable amount of Rs. 25,000 will be deemed to have been applied in the same year. However, the organization has to spend this amount of Rs. 25,000 in the year it is received or in the following year after receipt of the same, as the case may be.

There are also instances, where grants from donors are received by the end of the financial year, say, in the month of March. If so, compliance to the clause of utilizing 85% of the income received will not be possible. In such instances also, accumulation of income is

possible by applying to the Assessing Officer in Form 10 under Section 11 (2) within the prescribe time frame. It is important to state in the application that the amount falling short of 85% will be spent in the following year.

What happens to funds set aside for accumulation ? This is also specified in the Act.

4. Mode of Investment

Section 11(5) of the Income Tax Act, 1961 specifies the schemes in which the accumulated income has to be invested in order to avail the exemption. Though the time limit for making the investment is not specified in Section 11(2), paragraph 2 of Form 10 prescribes a time limit of 6 months for investing the accumulated income as per Section 11(5). The schemes include from Savings Account with a Scheduled Bank, Co-operative Society, Government Savings Certificate etc. The detailed list is provided at the end of this article. (Annexure-a)

5. Withdrawal of Exemption

In the following cases, the exemption will be withdrawn and the amount will be taxable at maximum marginal rate.

a. Application of income for other purposes – the exemption will be withdrawn if the accumulated income is spent for purposes other than for which it was accumulated.

b. Violation of Section 11(5) - In case an organization has made investment which does not comply as per Section 11(5), then the income from such unapproved investment would be subject to tax at the maximum marginal rate while the rest of the income would be exempt.

c. Non – Utilisation of accumulated income within the specified period : The income accumulated needs to be applied / spent within the specified period of 5 years.

d. Donation to other charitable organization –

As per the Finance Act, 2002, any donation given to another charitable organization out of the accumulated income will warrant withdrawal of exemption of the donor organization. Further, Finance Act, 2003 stated that inter-charity donation is possible only in the instance of dissolution of a charitable organization. Such donation is also to be made in the year of dissolution.

6. Conclusion

Voluntary Organisations have to, therefore, exercise utmost care in adhering to the above requirements relating to accumulation of income, violation of which will invite withdrawal of exemption and payment of tax.

Annexure-a

Modes of investment of Accumulated Income under section 11 (5)

The income accumulated under section 11(2) shall have to be invested in the modes specified under section 11(5) in order to avail exemption. The difference forms and modes of investing or depositing the money referred to it in clause (b) of sub-section(2) are provided as follows:

(1) Investment in savings certificates as defined in clause (C) of section 2 of the Government Savings Certificate Act, 1959 (46 of 1959), and any other securities or certificates issued by the central government under the Small Saving Schemes of the Government:

(2) Deposit in any account with the Post Office Saving Bank;

(3) Deposit in any account with a scheduled bank or co-operative society engaged in carrying on the business of banking (including a co-operative land mortgage bank or a co-operative land development bank).

Explanation.- In this clause, "Scheduled bank" means the State Bank of India constituted under the State Bank of India Act, 1955 (23 of 1955), a subsidiary bank as defined in State Bank of India (Subsidiary Banks) Act, 1959 (38 of 1959), a corresponding new bank constituted under section 3 of Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970 (5 of 1970), or under section 3 of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1980 (40 of 1980), or any other bank being a bank included in the Second Schedule to the Reserve Bank of India Act, 1934 (2 of 1934);

(4) Investment in units of the Unit Trust of India established under the Unit Trust of India Act, 1963 (52 of 1963);

(5) Investment in any security for money created & issued by the Central Government or the State Government.

(6) Investment in debentures issued by, or on behalf of, any company or corporation both the principal whereof and the interest whereon are fully and unconditionally guaranteed by the Central or by a State Government.

(7) Investment or deposit in any public sector company:

Provided that where an investment or deposit in any public sector company has been made and such public sector company ceases to be public sector company –

(A) such investment made in shares of such company shall be deemed to be an investment made under this clause for a period of three years from the date on which such public sector company ceases to be a public sector company;

(B) such other investment or deposit shall be deemed to be an investment or deposit made under this clause for the period up to the date on which such investment or deposit becomes repayable by such company;

(8) Deposit with or investment in any bonds issued by a financial corporation which is engaged in providing long term finance for industrial development in India & which is eligible for deduction under clause (8) of subsection (1) of section 36;

(9) Deposit with or investment in any bonds issued by a public company formed and registered in India with the main object of carrying on the business of providing long –term finance for construction or purchase of houses in India for residential purposes and which is eligible for deduction under clause (9) of subsection (1) of section 36;

(9a) Deposit with or investment in any bonds issued by a public company formed & registered in India with the main object of carrying on the business of providing long term finance for urban infrastructure in India.

Explanation- For the purposes of this clause,-

(a) “long-term finance” means any loan or advance where the terms under which moneys are loaned or advanced provide for repayment along with interest thereof during a period of not less than five years.

(b) “public company” shall have the meaning assigned to it in section 3 of the Companies Act, 1956 (1 of 1956);

(c) “urban infrastructure” means a project for providing potable water supply, sanitation and sewerage, drainage, solid waste management, roads, bridges and flyovers for urban transport.

(10) Investment in immovable property.

Explanation.- “immovable property” does not include any machinery or plant (other than Machinery or Plant installed in a building for the convenient occupation of the building) even though attached to, or permanently fastened to, anything attached to the earth;

(11) Deposits with the Industrial Development Bank of India established under the Industrial Development Bank of India Act, 1964 (18 of 1964);

(12) Any other form or mode of investment or deposit as may be prescribed [See sub- section (5) of section 11]

Rule 17C of the Income-tax Rules, 1962, prescribes the following forms or modes of investment or deposits by a charitable or religious trust or Institution under this Clause :

(1) Investment in the units issued under any scheme of the mutual fund referred

to in clause (23D) of section 10 of the Income tax Act, 1961;

(2) Any transfer of deposits to the Public Account of India; Deposits made with an authority constituted

in India by or under any law enacted either for the purpose of dealing with & satisfying the need for the

How to Design a Governance Manual for NGOs?

- Sanjay Patra, F.C.A., FMSF

&

- Madhuchhanda Mishra, FMSF

Every organization has a governance process which guides and controls the way it operates. In some organizations, these processes are formal and fairly well structured while in some others, they may be semi-formal. Again, there are some organizations where governance is very informal. It is also found that certain organizations do not make a distinction between governance and management as well.

It may be clearly said that having a clear defined governance process contributes to the overall efficiency of the organization. Each step /process needs to be documented and assimilated together. One of the reference tools for the internal governance of the organization is the 'Governance Manual'.

Governance Manual serves as a blue print for the governance of the organization

1. Purpose of the Governance Manual:

- i. Provides clarity to the Board members and the management about their roles and responsibilities.
- ii. Provides a clear distinction between Governance & Management
- iii. Serves as a blue print for governance of an organization

2. Broad Contents of the Governance Manual:

The Governance Manual should cover the following areas:

2.1. Strategic Direction of the Organization: One of the basic duties of an NGO's board is to provide strategic direction to the organization. This includes;

- defining organizational values and setting standards for professional conduct;
- identifying & articulating a clear mission statement;
- ensuring a common understanding of the mission within the organization;
- execution of the mission through appropriately planned activities & programs;
- regular reviewing of the mission to ensure it aligns with existing or planned activities.

All of these should be clearly stated in the Governance Manual.

2.2. Board members:

2.2.1. Roles & Responsibilities of Board Members:

The Governance Manual should clearly identify & put forth the roles & responsibilities of the board members. Even though the Board Members govern as part of a collective leadership, they have individual duties as well such as:

- Understanding & Supporting the organization's mission;
- Attending meeting regularly;
- Maintaining confidentiality;
- Offering informed & impartial guidance;
- Appointing the Chief Functionary.

A clear description of the roles & responsibilities of the Board Members in the Governance Manual would enable the members in internalizing their role and ensuring effective governance.

2.2.2 Election/Selection of Board Members: The manual should provide clear and concise guidelines

with regard to the election/selection of board members. The criteria for selecting board members, election procedures etc. need to be clearly stated in the 'Governance Manual'. Based on the Board's functions, including representing the various constituencies, the process of selection of Board members (and their designated Alternates) takes several criteria into consideration. All these issues should be addressed in the Governance Manual.

2.2.3 Term of the Board Members: The tenure of the Board Members should be clearly indicated in the manual.

2.2.4 Orientation of Board Members: Orientation is the processes of induction wherein new members integrate themselves into the overall organizational structure. Introducing new members to program, policies & strategic issues should form a part of the orientation process. The orientation of the Board Members can happen at three levels:

2.2.4.1. Verbal Orientation: Verbal Orientation by other board members on the various issues, policies, strategies, activities, mission, & vision of the organization would provide a basic idea to the new member about the organization.

2.2.4.2. Study of various documentation: The various documents such as vision mission statement, activity reports, financial statements, informational brochure or any other relevant document of the organization can be provided to the new board member.

2.2.4.3. Field Visits: The actual operation of the NGO can be understood by going to the field area. This would provide the new member with an overview of the ground reality. The basic guidelines about the orientation of a new board member should be provided in the governance manual.

2.2.5 Conflict of Interest: The issue of conflict of interest is of growing concern in NGOs and the governance manual should address this issue clearly. A conflict of Interest Policy should be in place in order to deal with a potential Conflict of interest situation.

2.2.6 Reimbursement: The service provided by the board members is voluntary and the position held by them is honorary. This is because it is crucial that board members do not derive, or be perceived as deriving, any direct or indirect benefit from their service in the board. However, reimbursement of travel expenses incurred for attending board meetings and other such expenses should be taken care of by the NGO. Further, if any of the specific skills of any particular board member are used by the NGO, then a reasonable compensation should be provided. The amount to be paid should be decided by the board in the absence of the concerned board member.

The service provided by the board members is voluntary and the position held by them is honorary

2.3. Board Meetings:

The Board should hold regular meetings to reflect and discuss on the performance of the organization and plan the future course of action. The Board meetings are also a platform for any strategic decision to be taken and any other issues that need to be dealt with. With regard to Board meeting, the Governance manual should at least include the following things:

2.3.1. Preparation & distribution of meeting

Agenda: For the Board meeting to be effective and fruitful, it is required that all the members are informed about the agenda for the meeting. This would help the members prepare for the meeting in advance and actively participate in the decision making process. The manual should specify this and clearly state the person responsible for the preparation and circulation of agenda.

2.3.2. Quorum: The Manual should specify how many members constitute a quorum (minimum, number of members that must be present to make the proceedings of a meeting valid), and the manner in which decisions are taken and recorded. Such guidance helps the board perform its tasks consistently and avoid doubts about the validity of its decisions.

2.3.3. Minutes: The record of board meetings is a basic instrument of accountability. Minutes are a form of institutional memory that enable an organization to work consistently. The board should ensure that a record of all formal proceedings, including their time and place, attendance, agenda, and decisions maintained.

2.4. Appointment & Appraisal of Chief

Functionary: The Board is responsible for appointing the Chief Functionary of the NGO and delegating authority to him for the overall management of the organization. It is the duty of the board to see that Chief Functionary fulfills all the required criteria and is fully capable of delivering the required job role. Further, the board should also ensure the accountability of the Chief Functionary by regular appraisals. It should also provide a clear and precise job description to the Chief Functionary which will enable him to understand his role more clearly.

2.5. Board Appraisal: The Board Appraisal is a process by which the board introspects and measures its own performance. These kinds of self-assessments help a board sharpen its understanding of leadership and define the contribution it can make to the NGO. Ideally, the board should set itself annual goals and measure its own performance against these targeted goals. The frequency and the procedure of the Board Appraisal should form a part of the Governance Manual.

2.6. Drafting and approving new policies: Since the board is primarily responsible for the governance of the NGO, it is therefore required that all the strategic issues pertaining to the NGO are clearly dealt with in the key policies of the organization. The board should ensure that all the key policies are well drafted and leave no room for doubt or confusion.

The broad contents described in above for the Governance Manual are by no means exhaustive. It just provides a brief overview of the major areas that need to be addressed in the Manual.

3. Who Should Prepare A Governance Manual?

The primary responsibility of preparing the Governance Manual is of the board. However, they should also receive necessary feedback from the Chief Functionary and other senior staff members.

4. Conclusion: As mentioned earlier, the Governance Manual is key tool for internal accountability. It should aim at precise demarcations between governance and management. It is a reference for the board members for their own conduct. A good Governance Manual provides clarity about the domain of operation for the board and hence is responsible for effective governance.

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A Critique of the Proposed Foreign Contribution Regulation Bill, 2006

- Manoj Fogla, F.C.A., Consultant

The fable goes that Alice in Wonderland kept on running for the entire day without covering even an inch of distance. The current Foreign Contribution (Regulation) Act, 1976 (FCRA) is a similar treadmill affair. Nobody knows what purpose this act has served in the last three decades. It is difficult to find even a single Non-Government Organization (NGO) being convicted for anti-national or subversive activity. But we did see cases being fought in Supreme Court for years together for innocuous acts such as legitimate money being received in a particular bank account. We did see dormant NGOs holding Foreign Contribution (FC) registration for decades together without filing returns and on the other hand NGOs with legitimate and approved project for enduring causes even today are running for prior permission and registration.

Recently, the Government proposed to replace the existing FCRA with the Foreign Contribution Regulation Bill 2006. The proposed bill continues to suffer from many fundamental as well as procedural shortcomings. There is an urgent need to revisit the relevance and rationale of this law.

1. The parameters for determining foreign source are irrational: Under the existing and proposed FCR (Foreign Contribution Regulation) law even companies like Infosys and HDFC Bank will be treated as foreign source because the foreign holding in these companies is more than 50%. In other words, an Indian NGO without FCRA cannot receive donations from these companies but if an NGO somehow manages to get FCRA, then it can receive funds from any country and any organization irrespective of the threats and security concerns involved in such receipts. The current norm of issuing licenses to receive foreign funds without bothering about the source needs to be revisited. Just imagine an NGO which was issued an FCRA registration 30 years ago filing nil returns has the potential to receive foreign fund from dubious sources

whereas a nationally recognized NGO (without FC registration) can not receive donations from a nationally recognized company. It may be noted that even for FDI (Foreign Direct Investment), the Indian Government has put certain countries under scrutiny scanner for security reasons. The Foreign Exchange Management Act (FEMA) notification. *The total foreign contribution received by India are around 7000 crore rupees and the bulk of such fund is contributed by handful of donors* No.20/2000 puts a ban on FDI inflow from certain countries and recently National Security Council has recommended some more to be added to that list. However, under the present FCRA, the source is not monitored at all.

2. Compelling reasons to make it donor specific: The mandate of the FCR law is to regulate the acceptance and utilisation of foreign contributions. The

The total foreign contribution received by India are around 7000 crore rupees and the bulk of such fund is contributed by handful of donors

total foreign contribution received by India are around 7000 crore rupees and the bulk of such fund is contributed by handful of donors. It remains inexplicable why for a meagre

1000 or 2000 crores (contributed by small irregular donors) the FCR donor fraternity has been kept open ended. Anybody from anywhere can send any amount into India. It may be noticed that under the current Act also around 104 foreign organisations are not treated as foreign source. Similarly, all time-tested donors should be added to this list and the remaining irregular or dubious donors should be subjected to prior permission or scrutiny. *Why should we allow*

even a FC registered NGO to receive funds from an unrecognised or dubious source ? The threat of terror and antinational activity would be negated to a large extent if the foreign contribution is accepted only from the time tested donors and all the remaining donors should be subjected to prior permission. With one simple regulation the unmanageable task of needlessly monitoring 20000 NGOs from a threat perspective could be rationalised.

The regulation of the NGO sector is a much larger issue than what FCRA can service. It is estimated that around 3% of GDP is mobilised and utilised through the NGO sector and FCRA funds happen to be only 0.15% of the GDP. Therefore, the terror angle and the regulation angle should not be mixed and *FCRA is the royal scion of the foreign currency starved era of the 70s and 80s* stand alone policies and rules should be formulated. If the entire NGO sector needs to be regulated then not only the FC component should be monitored which is only 5 to 6% of it, as 95% would still remain unregulated

3. The FCRA was enacted when the needs of India were different: When the FCRA was enacted, our country was starving for foreign exchange. The foreign exchange generated through contributions was much more than the foreign direct investments. It is surprising to note that in the first 4 decades after our independence we were not able to generate even 1 billion dollar of FDI. Today TATA alone invested in excess of 12 billion dollars in the Corus takeover deal. There has been a radical transformation as far as our economic and fiscal standing is concerned. FCRA is the royal scion of the foreign currency starved era of the 70s and 80s. In those days funds received through contributions used to form a substantial chunk of the total foreign exchange inflow. Therefore, one can understand the mindset of government in 1976 and its inability to propose any restriction on the donors and the source. But today FCRA contribution

does not form even one percent of the total foreign exchange movement or even the foreign exchange reserves. If terror funding has to come it will not single out NGOs. Ironically as per an article in Economic Times dated 18th July 2007 by Swaminathan S Anklesaria Aiyar, the RBI is unable to provide detail of foreign fund receipts to the

FCRA is the royal scion of the foreign currency starved era of the 70s and 80s

extent of 23.6 billion dollars received under small business receipts. India has not received 23.6 billion dollars from contributions even in last 30 years. If the one year suspense account of foreign funding is 23.6 billion dollars why the scanner is only 1.5 billion dollars received as foreign contributions from mostly the known donors. There is a need for a wider understanding and approach to this issue.

4. Irrational cap on administrative expenses:

The proposed law provides for a maximum of 50% in administrative expenditure. The 50% cap on administrative expenditure again is an irrational provision which reflects absence of accounting understanding. If by administrative expenditure the authorities imply expenditure in the nature of salary, travel, etc. then it will be highly erroneous. For example, the salary of a doctor in a health project cannot be termed as administrative in nature. There may be NGOs where most of the expenditure is in the shape of salaries, travel, publishing etc. but still the administrative expenditure could be negligible.

5. Restriction on investment overriding section 11(5)

of Income Tax Act: The proposed law provides that no investments could be made in equity linked instruments. Such provisions will have a needless overriding effect on the provisions such as section 11(5) of the Income Tax Act, which regulates the investments permissible for charities.

6. Monitoring of asset created: The proposed law provides that any asset created from foreign funds shall be disposed in accordance to the FCRA which may specify such authority or manner of disposal. It need to be understood that project grants are inherently capital receipts whether assets are created or used otherwise. This provision again will create undue hardship to the NGOs, because firstly the term asset can be very misleading as a chair or a calculator are also considered as assets. Secondly NGOs are involved in developing project assets and community assets which are legally bound by the project agreement as far as retention or disposal is concerned.

7. The proposed law is unjust and unfair to Community Based Organizations (CBOs) and village level NGOs: The proposed law fails to address the travails of small community based village level organizations which do not have the ability to procure FCRA registration. In the past three decades the FCRA has done great dis-service to the nation by preventing the money from reaching to the grass-roots. The small and medium NGOs do not transfer money to small village level organizations under the pretext of FCRA. It is necessary that some exemptions or monetary limits are provided for such small organizations for receiving foreign funds as second recipients.

John Maynard Keynes once said that Man will do rational things only after exhausting all other possibilities. In the backdrop of the above discussions one wonders why this treadmill run still continues. Why should we put such high premium on rational behavior?

The Micro - Financial Sector (Development & Regulation) Bill, 2007 – Key Features & Highlights

- Research Team, FMSF

The Finance Minister, Mr P. Chidambaram, tabled the Micro Financial Sector (Development and Regulation) Bill 2007, in the Lok Sabha on March 2007. The Bill makes the National Bank for Agriculture and Rural Development (NABARD) the regulator for the micro-financial sector. The enactment of the Bill aims to ensure a legal framework for entities engaged in micro-finance and facilitate an environment for development of micro-finance services in the country with greater transparency, effective management, and better governance. It also seeks to facilitate the flow of micro-finance services to un-banked population in the country. This article highlights some of the provisions & key features of the Bill.

Microfinance is considered as a potent tool to counter poverty the world over. The term “Microfinance” can be defined as “provision of thrift, credit and other financial services and products of very small amounts to the poor in rural, semi urban or urban areas, for enabling them to raise their income levels and improve living standards” (NABARD 99) The Indian microfinance sector is characterized by a diversity of strategies, methodologies, organizations, partnerships and performance.

In the light of the above said, the Micro Financial Sector (Development & Regulation) Bill, 2007 seems to be of much importance & significance. The bill seeks to promote and regulate Micro Financial Organizations (MFOs).

The preamble of the bill sets the objective which is “to provide for promotion, development and orderly growth of the micro financial sector in rural and urban areas to facilitate universal access to integrated financial services by the population not having banking facility and thereby securing prosperity of such areas and regulation of the micro finance organizations not being regulated by any law for the time being in force and for matters connected therewith or incidental hitherto”.

Key Features:

1. Regulation: NABARD is designated as the regulator of the micro financial sector. However, its dual role as a key participant in the sector and the regulator could lead to conflict of interest.

NABARD shall promote and ensure the orderly growth of the micro financial sector. It may;

- formulate policies for transparency and good governance;
- set sector related benchmarks on methods of operation;
- facilitate the development of credit rating norms; and
- specify accounting and auditing norms for MFOs

The National Bank has the power to issue directions from time to time if it is of the opinion that such directions are necessary, in the public interest or in the interest of the policy relating to micro finance organizations.

1.1. Power to Issue Directions: The National Bank has the power to issue directions from time to time if it is of the opinion that such directions are necessary, in the public interest or in the interest of the policy relating to micro finance organizations. The MFOs are bound to comply with the directions. NABARD also reserves the power to modify or cancel any of its given directions as well.

1.2. Inspection: NABARD may authorise an inspecting authority to inspect any MFO and

submit a report. If NABARD considers that an MFO's operation is harming eligible clients, it may take appropriate action including winding up of the MFO. The MFO shall be allowed to make a representation with regard to the report.

2. Registration:

Every MFO that offers thrift services to eligible clients needs to obtain a certificate of registration from NABARD. As per the act, any micro finance organization which is offering thrift services, before or at the time of commencement of the Act will have to apply for registration in writing to the National Bank before the expiry of six months from the commencement of the Act. The registration certificate may be granted by NABARD if certain conditions are met such as

- the general character of the management is not prejudicial to the interest of eligible clients;
- the net owned funds of the MFO is at least Rs 5 lakhs;
- The MFO has been in existence for at least three years.

NABARD may cancel the registration if an MFO ceases to provide thrift services or fails to comply with any of the conditions on which the registration was granted or any direction issued by NABARD or does not submit account books or other documents for inspection.

However, no applicant will be rejected without an opportunity of being heard.

2.1. Cancellation of Certificate of Registration: NABARD may cancel the registration if an MFO ceases to provide thrift services or fails to comply with any of the conditions on which the registration was granted or any direction issued by NABARD or does not submit account books or other documents for inspection. An MFO may be granted time to comply with NABARD's directions if it is not against public interest or the micro financial sector or eligible clients. If an MFO violates any prescribed provision, NABARD may also prohibit such MFO from accepting thrift. However, the MFO would be given the opportunity of being heard.

3. Reserve Fund: Every MFO has to create a 'Reserve Fund' by transferring a minimum of 15% of its net profit or surplus realized out of thrift services and micro finance services. The National Bank may direct the organization to invest the part or whole of reserve fund in unencumbered securities as may be specified in the regulations

4. Micro Finance Development Council (MFDC): The Central Government may establish a MFDC to advise NABARD on formulation of policies related to the micro-financial sector.

5. Micro Finance Development & Equity Fund: NABARD shall constitute a Micro Finance Development and Equity Fund to be utilized for the development of the micro finance sector. The Fund would include (a) all grants received from the government and other sources; (b) any income received from investments made in equity of an MFO; and (c) the balance outstanding in the Fund maintained by NABARD before the commencement of the Act.

The Fund would be managed by the Board of Directors of NABARD and would be used to provide

any financial assistance to an MFO, invest in equity of an MFO, and meet any other expenses for the promotion of the micro finance sector

6. Redressal Mechanism:

6.1. Ombudsman: NABARD in consultation with the MFDC may appoint a micro finance ombudsman. The micro finance ombudsman may provide for:

a) Appointment, terms of office, conditions of service, location of office of the ombudsman;

b) Nature of grievances and complaints that may be entertained and the procedure for redressal of grievance;

c) Any other matter that may be necessary for effective functioning of ombudsman.

6.2. Offences & Penalties:

S.no	Offences	Penalties
1.	Willful omission or making false statement in application, declaration, return, statement, information, or particulars made	Imprisonment for term which may extend to two years and liable to fine.
2.	Contravention or default in complying with the requirements of the Act Where the contravention is a continuing one	Punishable with fine that may extend to twenty thousand rupees. A further fine which may extend to one thousand rupees for everyday during which the default continues and imprisonment for a term not exceeding two years or with both.
3.	Failure to comply with the provisions or order of the Micro finance ombudsman or of orders of the Central Government.	Imprisonment which may extend to three years and liable to fine of not less than five hundred rupees for every day during which the non-compliance continues

7. **Returns:** Every MFO, whether engaged in providing thrift services or not at the commencement of the Act, shall file a return containing particulars of its activities in the form and manner as prescribed within ninety days from the date of commencement of this Act with the National Bank. The returns shall be duly certified by a Chartered Accountant or a Company Secretary or an auditor appointed by the Registrar of Co-operative Societies of the State.

8. **Special Audit:** If the National Bank is of the opinion that it is necessary in the public interest or for the purpose of proper assessment of the records and books of account of the micro finance organisation, it may direct the auditor to audit the accounts of the micro finance organisation in relation to any transaction for such period or periods as may be specified in the order. The auditor shall comply with directions and make a report of the audit. He shall report it to the National Bank and forward a copy thereof to the micro finance organization. He shall have the power to exercise the functions and discharge the duties and be subject to the liabilities and penalties imposed on him by virtue

of section 227 of the Companies Act. The expenses of the audit shall be borne by the micro finance organisation.

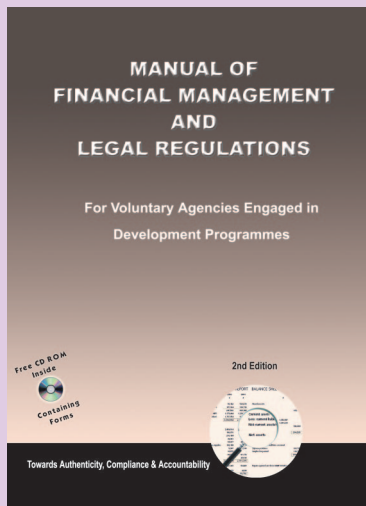
9. **Usurious Loans Act, 1918:** The Bill does not exempt registered MFOs offering thrift services from the Usurious Loans Act, 1918 or state laws which prohibit charging of excessive interest rates (such as Tamil Nadu Money Lenders' Act, 1957, Kerala Money Lenders' Act, 1958). This could lead to dual regulation of MFOs offering thrift services. The rate of interest charged by banks is exempted from the Usurious Loans Act, 1918 and any other law related to indebtedness in force in any state.

The Micro Finance sector in India has not reached its full growth even 15 years after its emergence in the early nineties. One of the possible reasons could be the lack of uniform regulations and slow policy processes. The bill can be seen as a step forward in the process of bringing about uniform regulations. However, the success or failure of the Bill can only be appropriately assessed after its implementation.

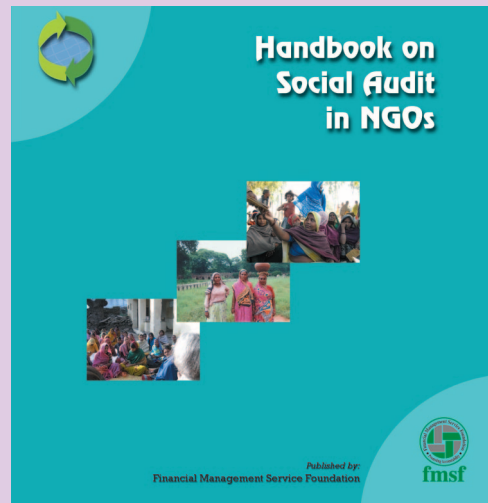
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1. www.indiatogether.org
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3. www.thehindubusinessline.com

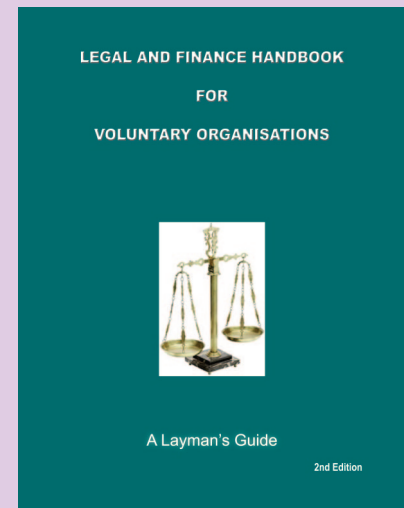
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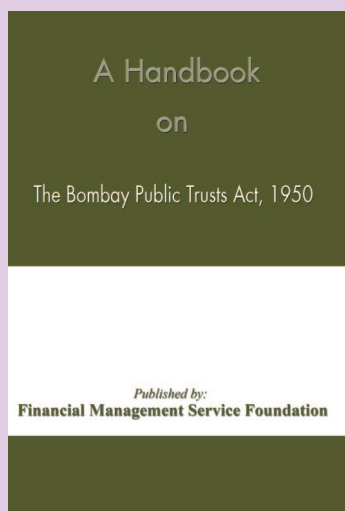
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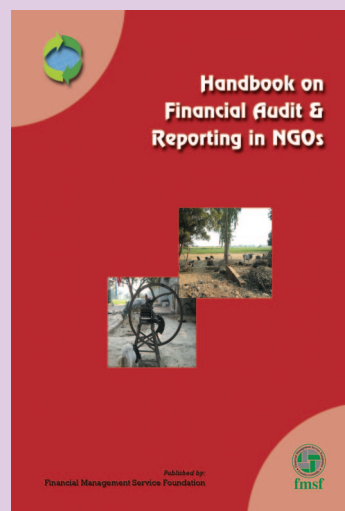
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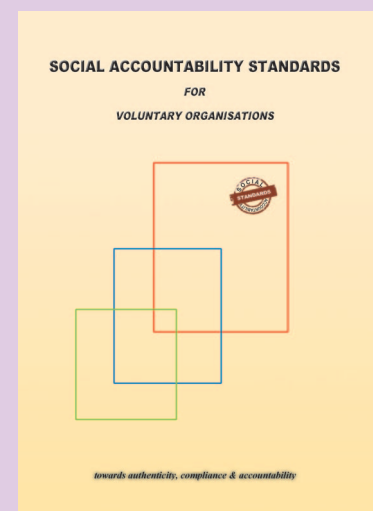
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